

BEFORE THE BOARD OF LAND COMMISSIONERS AND
THE DEPARTMENT OF NATURAL RESOURCES
AND CONSERVATION OF THE STATE OF MONTANA

In the matter of the amendment of) NOTICE OF AMENDMENT
ARM 36.25.110 regarding the rental)
rate for state grazing leases)

To: All Concerned Persons

1. On August 11, 2011, the Department of Natural Resources and Conservation published MAR Notice No. 36-22-148 regarding a notice of public hearing on the proposed amendment of the above-stated rule at page 1479 of the 2011 Montana Administrative Register, Issue No. 15.

2. The amendments to the rule are reasonably necessary to obtain the current full market value of grazing forage on state school trust lands while providing for prudent management of these grazing resources and they allow the board to obtain sustainable long-term revenue for the trust beneficiaries. The reduction in the multiplier from 13.18 to 11.65 reflects and recognizes the contractual duty of the lessee to control noxious weeds and the cost of that function. A further reduction in the multiplier from 11.65 to 10.48 serves to encourage the use of rest-rotation grazing and it reflects the uncertainty of forage being available for use due to drought and other natural weather conditions. The provision allowing a lessee to apply to the department for a 50% reduction where forage is unavailable for use acknowledges that where forage cannot be put to any economic use it should be subject to a lesser rental rate. The five-year phase-in provision for an increase in the minimum grazing rental rate allows the board to obtain the full market value for these trust assets while allowing the grazing lessees to economically adjust their operations to this increase over a reasonable period of time.

3. The department has amended ARM 36.25.110 as proposed, but with the following changes from the original proposal, new matter underlined, deleted matter interlined:

36.25.110 MINIMUM RENTAL RATES

(1) and (2) remain as proposed.

(3) The rental rate for all grazing leases and licenses shall be on the basis of the animal-unit-month (AUM) carrying capacity of the land to be leased or licensed. The minimum annual rental rate per AUM is the weighted average price per pound of beef cattle on the farm in Montana as determined by the Montana Agricultural Statistics Service of the U.S. Department of Agriculture (USDA NASS) for the previous year, multiplied by: ~~13.18.~~

(a) 8.13 in calendar year 2012;

(b) 8.72 in calendar year 2013;

(c) 9.3 in calendar year 2014;

(d) 9.89 in calendar year 2015; and

(e) 10.48 in 2016 and all calendar years thereafter.

(4) A lessee may nominate to the department a tract of land containing grazing acres to be placed into a nonuse category.

(a) In order to qualify for the nonuse category:

(i) the nomination must be for the entire or remaining portion of a lease term, and the lessee must agree that no livestock use shall occur during that time; and

(ii) the grazing lands must be intermingled with agricultural acres in the tract, or otherwise possess characteristics which prohibit livestock use.

(b) All nominations are subject to review and approval by the department. If the nonuse is approved by the department, beginning in 2013 the annual rental rate charged for the grazing acres shall be one-half the amount calculated under (3), and shall become effective in the next billing cycle.

(4) through (7) remain as proposed but are renumbered (5) through (8).

4. A summary of the written comments and oral testimony from the four hearings held between September 12 and September 15, 2011, appears below with the department's responses.

COMMENT 1: DNRC received 62 comments in support of the proposed rules.

RESPONSE 1: DNRC appreciates the interest in this rulemaking process.

COMMENT 2: Commenters said that state lands grazing leases are not for exclusive use. State grazing leases are subject to recreational use (which can result in damage to improvements), oil and gas development, logging, use by easement holders, and gravel permits, which is typically not the case with private leases. Ergo, a comparison to private leases is not appropriate.

RESPONSE 2: All state leases are issued with a provision that DNRC reserves the right to issue permits for other uses on the land. If those uses conflict with or limit grazing utilization, DNRC will adjust and reduce the carrying capacity accordingly. DNRC believes that many nonexclusive situations occur on private grazing leases as well. For example, if the surface owner who has leased out grazing does not have the mineral rights to that property, mineral development may occur. DNRC is also aware that landowners may lease grazing to one individual and outfitting to another.

COMMENT 3: In setting the multiplier, DNRC should consider the cost of weed control that a lessee must pay for full suppression.

RESPONSE 3: The issue of weed management is an area that DNRC closely monitors when completing renewal inspections for leases. Staff may require a lessee enter into a weed management plan that specifically outlines the steps a lessee will use to manage and control weeds. Given the important nature of controlling weeds to protect long-term productivity of the lands, DNRC agrees and has reduced the multiplier to account for costs incurred by lessees.

COMMENT 4: Commenters stated DNRC should account for the fact that a lessee must pay the full grazing rental even if the AUMs are not utilized. Reasons for nonuse include drought or insects, fire, if the lessee is in a rest/rotation grazing system, or if the state land is contained within a Bureau of Land Management (BLM) allotment.

RESPONSE 4: The previous two multipliers set by the board did account for periodic nonuse during a lease term. For areas where grazing lands are intermingled with crop land and not used, or topography or other features restrict use, the board has amended the rule so that a lessee may be allowed to nominate those lands for nonuse for the entire lease term and only pay a grazing rental at half the new rate. The board has also reduced the multiplier to encourage rest-rotation grazing and to recognize that forage may be occasionally reduced due to drought or other natural conditions.

COMMENT 5: Commenters spoke of costs of improvements to the state land borne solely by the lessees. Most commenters focused on fencing and water improvements, and many provided actual costs associated with those improvements. Many noted the fact that the costs associated with improvements have outpaced the returns they are receiving for their livestock. In addition, improvements such as water developments benefit wildlife as well.

RESPONSE 5: DNRC agrees that the state does not share in the cost associated with the development of water, fencing, and other livestock improvements. In the recommendations of the 2011 Duffield study, this is the primary basis for the reduction of 30% from the private lease rate.

COMMENT 6: Commenters stated the comparison between state and private lease rates is not appropriate.

RESPONSE 6: Under 77-1-106, MCA, the board must consider the trust asset and be in the best interests of the state with regard to the long-term productivity of the school trust lands, while optimizing the return to the school trust. DNRC believes that fair market value can be achieved by looking at private lease rates with adjustments made for lessee expense as required under this statute.

COMMENT 7: Commenters stated Duffield's recommendation of a 30% reduction to account for differences between a private and state lease was not adequate. Commenters noted costs for water developments, fencing, rangeland renovation, type of pasture, the security of state lease, costs of livestock management, costs of fire suppression, costs of salt and others. Some commenters included lease-specific costs while others referred to studies that discussed costs for public and private leases.

RESPONSE 7: The work in the Duffield report relied on three primary sources of information to support the recommendation that state leases should be approximately 70% of the private rate. Those were: the Hedonic model; the

average competitive bid rate for state leases; and the 1998 report by Torell et al. The model was intended to identify characteristics of leases that influence the prices paid for them. The characteristics identified included location; whether the lease was new (less than one year old); terms (length); whether fence maintenance or water development was provided by the lessor; and land type (dryland or irrigated). Other characteristics such as in-holdings, productivity, and operating expenses were not included in the model because they did not add to it given the characteristics noted above. Duffield's work also noted that competitive bids on state lands averaged 78% of the private rate and that the Torell study found that approximately 30% of the private lease rate was the amount paid for services.

COMMENT 8: Commenter stated there is a substantial difference in private versus state lease rates in the fact that private lease rates are standalone units and state lands are not.

RESPONSE 8: DNRC recognizes that state leases represent a variety of ownership patterns. Some tracts represent in-holdings contained within larger pastures, some make up individual pastures themselves, while other state blocks have several pastures. The Duffield study noted that in its statistical model, in-holdings did not add any predictive power given the other identified variables.

COMMENT 9: Commenters suggested that the 2011 Duffield study was not appropriate to use because it did not use the data gathered by the 1993 and 1994 advisory council; it was based on the original study that was rejected by the 1993 Legislature; or because it was based on a previous study that the board rejected.

RESPONSE 9: The original 1993 Duffield report represented significant work in estimating full market value for various uses on state lands. Because of the controversy surrounding those recommendations, SB424 was passed by the 1993 Legislature directing the Land Board to set rental rates after first taking recommendation from an advisory council they appointed. Although the advisory council elected to base their grazing rate recommendations on other factors, they did adopt the recommendations of the Duffield report for recreational use on state lands. DNRC feels both the 1993 and 2011 work contain relevant information relevant to the rulemaking.

COMMENT 10: Commenters stated Duffield's use of competitive bidding to establish the value of forage is not appropriate because it does not consider what value the bidder is attributing to the long-term addition of those lands to their operation as well as other possible benefits for the livestock owner.

RESPONSE 10: While DNRC agrees that the motivation for competitive bidding may involve many factors, it does fundamentally give an indication of the underlying value of that forage and lease. If competitive bids were being

used as the sole basis for justifying an increase to the multiplier, further study into the individual characteristics might be warranted. Competitive bidding is only one factor in the supporting evidence utilized by the board in setting the multiplier for the minimum grazing rental rate.

COMMENT 11: Commenter suggested that the quality of forage in the Great Plains states Duffield used in the study is not comparable to Montana.

RESPONSE 11: DNRC agrees that the rental rates charged in the plains states may not, for various reasons, be directly applicable. DNRC does not agree that forage quality in the plains states is superior to that found in Montana.

COMMENT 12: Commenter was concerned with the work utilized in the Duffield study on the BIA AUM rates. In particular, very little data was given to support these rates and what services these leases provide.

RESPONSE 12: The statements that BIA leases are similar to state leases were first noted in the 1993 Duffield report.

COMMENT 13: Commenter said the Duffield study stated that the BLM/United States Forest Service (USFS) rate was subsidy, and therefore the rate was removed from the comparison and that this statement was conjecture on the part of the study.

RESPONSE 13: The Duffield report stated that the federal rate may be intended to provide a subsidy based on a 2005 Government Accountability Office (GAO) report.

COMMENT 14: Commenter stated the proposed multiplier could result in significantly higher rates in the near future (\$15 to \$17 per AUM) due to increasing cattle prices.

RESPONSE 14: The basis for the existing formula is that prices received should be reflective of a lessee's ability to pay. If the board adopts a multiplier of 13.31, the average price per pound of beef cattle would need to reach \$1.13 per pound for the AUM to be \$15.00/AUM.

COMMENT 15: Commenters stated the proposed multiplier fails to consider profit margin and that ranchers will lose money if the multiplier is raised to this level. The operational costs required to harvest forage are increasing much faster than the prices received for livestock.

RESPONSE 15: 77-1-106, MCA, outlines what factors the board should consider in establishing rental rates. To date those costs have been specific to improvement costs associated with utilization of the lease. Given the wide

variety of types of livestock operations in the state, DNRC does not agree that the rental rate should use profit margin in this analysis.

COMMENT 16: Commenter suggested the Duffield study does not recognize the fact that private leases are competitively bid while 95% of state leases are not competitive bid.

RESPONSE 16: DNRC disagrees in that state leases are available for competitive bidding when they are issued or renewed. There are many reasons why a lease may or may not receive bids. The intent of the grazing rate formula is to ensure that full market value is being achieved if no competing bids are submitted.

COMMENT 17: The Duffield study is biased in the sense it first determined a conclusion, and then found evidence to support that conclusion while ignoring that evidence that did not support the predetermined conclusion.

RESPONSE 17: DNRC disagrees. The original work by Duffield in 1993 used extensive survey information along with a statistical model to estimate what characteristics influence the values of grazing lease rates. The current study was intended to consider updated information to provide DNRC with an estimate market value for state leases.

COMMENT 18: The Charles M. Russell Wildlife Refuge increased their rental value to \$18.40/AUM a number of years ago which has resulted in an increase in the number of vacant CMR allotments. The 2011 Duffield report did not consider that the same could occur on state land.

RESPONSE 18: The Duffield study suggested that the wildlife refuge rates may support a state land rate higher than 70% of the private rates, although it was acknowledge that federal leases may provide more services than under a state lease.

COMMENT 19: Commenters suggested the private lease rate that Duffield utilized was inaccurate. The value does not consider that as a private lease term goes on, the value often goes down. As a result the multiplier that has been recommended is an arbitrary number.

RESPONSE 19: The private lease rate as reported by Montana Agriculture Statistics is an average lease rate. This average lease rate would include values with various factors including the length of the existing lease. As such, DNRC believes that it is a representative value.

COMMENT 20: Commenter suggested the forage grown on state land is generally not comparable in quality to that harvested off of private land and therefore, the Duffield comparison is not appropriate.

RESPONSE 20: State land ownership generally includes sections 16 and 36 of each township, as well as other blocks and individual parcels around the state. Because of this random ownership, it is a true representation of the landscapes present across the state. Some lands may be of poorer quality while others are extremely productive, and collectively would be of average production. As such, DNRC disagrees with the claim that the rental rate should be lower due to the poor quality of the lands.

COMMENT 21: Commenters addressed how the carrying capacity is set and used on state lands. Particularly, the allocation of AUMs (based on a 1000-lb cow) and a rancher's use of the AUM (cows weigh between 1300 and 1500 lbs). Questions were raised that actual livestock usage would not support DNRC-assessed AUMs.

RESPONSE 21: DNRC utilizes Natural Resources Conservation Service's (NRCS) Montana Grazing Guides to determine rangeland condition and the stocking rate or carrying capacity. The range guides use specific factors including topography, precipitation zone, soil type, and the existing native vegetation to determine range sites. Existing vegetation on each range site is compared to climax vegetation on each range site to determine range condition. Range condition is the present state of the vegetation compared to the kind and amount of native vegetation that site is capable of producing (MSU Mont. Guide MT198515 AG). AUMs per acre are then calculated by percent of climax vegetation multiplied by the suggested initial stocking rate.

77-6-507(1)(a), MCA, defines "animal unit" as one cow, one horse, five sheep, or five goats. Section (b) further defines "animal unit month carrying capacity" as that amount of natural feed necessary for the complete subsistence of one animal unit for one month. The animal unit month (AUM) is the basic unit of grazing capacity and is defined as the potential forage intake (animal demand) of one animal unit for one month (Vallentine – grazing management 1990). The Society for Range Management defines an animal unit as one mature 1000-lb cow.

DNRC has found that when monitoring pastures where AUM utilization was known, this system is generally conservative in the carrying capacities that are calculated. DNRC believes if AUMs are utilized in accordance to the lease agreement, the range will maintain good condition and continue to sustainably support livestock grazing, even given the difference between the statutorily defined animal unit and the definition used by range science professionals.

COMMENT 22: Commenter discussed the ramifications of increasing/doubling the rate. If fees are raised, there may be a significant increase in vacancies which will result in decreased revenues and DNRC will lose good stewards of the land. Also since many tracts do not have public access, they may remain vacant and DNRC will be liable for costs associated with those lands (weed control or fencing out livestock).

RESPONSE 22: DNRC recognizes that raising the rental rate may result in increased vacancies. If vacancies occur, DNRC will attempt to release those lands. For any lands that remain vacant, DNRC will be responsible for any associated management costs.

COMMENT 23: Commenters stated DNRC needs to consider how the forest management Habitat Conservation Plan (HCP) and the USFW Comprehensive Conservation Strategy impact grazing leases

RESPONSE 23: DNRC's HCP is only applicable to grazing licenses on forested lands within the HCP project area. The primary commitments apply to bull trout, westslope cutthroat and redband trout, which are found on less than 2% of the total grazing area. These commitments are actually very similar to those previously adopted in 1996 in the State Forest Land Management Plan. If any grazing management issues are identified on those tracts, DNRC will work with lessees to address them. However, given the very small percentage of acreage this affects and because these commitments are already being implemented, DNRC does not believe adjustments to the rate are warranted for this issue. The USFW Comprehensive Conservation Strategy has not been adopted by DNRC, nor has DNRC had involvement in that plan.

COMMENT 24: Commenters suggested the current formula and multiplier is fair and ensures that the rate increases when livestock prices increase.

RESPONSE 24: The current formula is established in statute and requires the board to set the multiplier used to calculate the annual rental. Under 77-1-106, MCA, the board must optimize the return to the trusts while considering long-term productivity and expenses borne by the lessee when setting the multiplier. The recent work by Duffield suggests that the current multiplier does not achieve full market value, and was the basis for initiating the rulemaking process.

COMMENT 25: Commenters suggested the board should be at the rule hearings, listen to the tapes of the meetings, review all of the submitted written comments, reject the Duffield studies, appoint an advisory board, commission a new study, meet with randomly selected lessee to discuss costs, and take more time to understand issues.

RESPONSE 25: DNRC conducts the administrative rulemaking process on behalf of the board. The rulemaking process allows for comments and information to be submitted, and all information from that process is made available for the board to consider and review in order to determine what may be relevant for their decision.

COMMENT 26: The board is required by law to consider lessee's expenses, and to meet their legal fiduciary responsibilities.

RESPONSE 26: DNRC agrees, as this is required under 77-1-106, MCA.

COMMENT 27: The board needs to ensure recreationists are paying full market value for recreating on state lands.

RESPONSE 27: The board may at any time review rentals being charged for various uses to ensure full market value is being received. Recreational use fees were last reviewed in 2007, while the grazing multiplier was last updated in 2001. Recreational use fees are beyond the scope of this rulemaking process.

COMMENT 28: The last two previous increases by the Land Board were approximately 12% each. An increase of 75% as proposed would be a significant burden for lessees and will result in less monies being available for improvements and conservation measures.

RESPONSE 28: The board is responsible to ensure that the trusts receive fair market value regardless of the percent increase that may result.

COMMENT 29: The board should defer the grazing rental rate to a ballot initiative in order to remove politics from the process.

RESPONSE 29: The responsibilities and duties of the board are established in Article X, Section 4 of the Montana Constitution. Additionally, under 77-6-507, MCA, the board is responsible for establishing the multiplier used to calculate the annual grazing rate. These responsibilities cannot be transferred to a ballot initiative.

COMMENT 30: The board should phase the rate increase in over a ten-year period in order to allow lessees to budget and acclimate to the change.

RESPONSE 30: Under 77-6-502(2), MCA, and the terms of the lease agreement, any increased rental enacted by the board may become immediately effective for the lease. The board agrees that a five-year phase-in of the minimum grazing rate is appropriate to allow lessees to economically adjust to the rental increases.

COMMENT 31: Such an increase will result in damage to the resource because lessees will always be compelled to use the AUMs they have been paying for, and because a rate increase reduces the monies that are available to a lessee to make improvements to a lease.

RESPONSE 31: As discussed in previous responses, the process DNRC uses to establish carrying capacities results in fairly conservative numbers. On a case-by-case basis, if grazing management problems develop as a result of the lessee utilizing the set carrying capacity, DNRC will work with the lessee to address or adjust those issues.

COMMENT 32: Commenters stated lessees pay for AUMs that wildlife use.

RESPONSE 32: The carrying capacity established by DNRC is typically conservative and should allow for general wildlife use without impacting the lessee's ability to utilize the AUMs they pay for. On site-specific cases where concentrated or heavy wildlife use is occurring, DNRC can adjust the carrying capacity to account for that use.

COMMENT 33: DNRC is required to comply with the Montana Environmental Policy Act (MEPA) in the rulemaking process.

RESPONSE 33: DNRC agrees. A MEPA analysis utilizing the public hearings is being conducted.

COMMENT 34: Commenter suggested that leases of any value are already competitively bid.

RESPONSE 34: DNRC disagrees. In general, competitive bidding of state leases amounts to less than 5% of the annually renewed leases. There are a number of possible reasons why this is rather low, including location and access to the lease, the preference right of existing lessees, or the reluctance to bid against neighbors. As such, many productive and desirable leases receive no bids at renewal.

COMMENT 35: Commenter said the current formula overprices the state AUM rate.

RESPONSE 35: DNRC has received no evidence that supports that the current rate is above full market value, or that resultant vacancies exist.

COMMENT 36: Commenter stated that in areas where significant acreages of state lands exist, doubling the rate will negatively affect the local economies.

RESPONSE 36: Daniels County has the largest percentage of state land. If the board adopted the multiplier as proposed, the total increase in grazing rentals would be approximately \$188,000, or an average of approximately \$280 per lease.

COMMENT 37: Commenter said that doubling the fee will force the Department of Fish, Wildlife and Parks (FWP) to increase license fees in order to pay for their state land leases.

RESPONSE 37: As with any lessee, FWP's possible actions to pay increased grazing rentals is beyond the scope of DNRC rulemaking.

COMMENT 38: Commenter suggested doubling the fee could force landowners to charge access fees to recreate on their private land in order to raise the necessary funds to pay the increased rentals on state land.

RESPONSE 38: Although this may be an action implemented by some lessees, the board is constitutionally required to ensure full market value is being received for uses on state land.

COMMENT 39: Commenter asserted that a lessee has acquired under the provisions of the 1866 Mining Act (14 U.S. Statute 252, Revised Statute 2339) water rights upon various parcels of state lands which pre-date the state's ownership, and which in turn, grant fee simple title of those parcels to them.

RESPONSE 39: DNRC disagrees with this legal analysis. Although DNRC acknowledges that water and ditch rights established on state trust lands prior to the state's acquisition of title could theoretically encumber state title to such lands, such rights would not divest the state of the fee simple title to those lands.

Section 9 of the 1866 Mining Act (Revised Statutes 2339 and 2340) provided only for the acquisition of water rights and ditch rights upon federal public lands:

"Whenever, by priority of possession, rights to the use of water for mining, agricultural, manufacturing, or other purposes, have vested and accrued, and the same are recognized and acknowledged by the local customs, laws, and the decisions of courts, the possessors and owners of such vested rights shall be maintained and protected in the same; and the right of way for the construction of ditches and canals for the purposes herein specified is acknowledged and confirmed;..."

"All patents granted, or preemption or homesteads allowed, shall be subject to any vested and accrued water rights, or rights to ditches and reservoirs used in connection with such water rights, as may have been acquired under or recognized by this section".

A state grazing lease provides livestock forage for the use of a lessee on a designated parcel of trust land. DNRC does not warrant title to the ownership of its lands or the water rights upon those lands. An applicant for a grazing lease has the obligation to review the title to the trust lands offered for lease and determine whether to bid upon them. No one is obligated to lease trust lands. Lessees may review the title to the trust lands that they lease and make their own decisions as to whether they should continue to lease those trust lands. Nonetheless, a determination of the quantity, ownership, and priority date of water rights upon state trust lands is beyond the scope of this rulemaking.

COMMENT 40: Commenters stated BLM allotment managers do not recognize the carrying capacity for state lands that are included in the BLM allotments. If the state ratings are higher than the BLM ratings, the lessee is paying for unusable forage.

RESPONSE 40: Based on discussions with BLM staff, DNRC's carrying capacities are generally considered and used for the state lands contained within BLM allotments. In situations where they are not, a lessee may request that DNRC

review and further discuss with BLM staff, the appropriate carrying capacity for the state lands.

COMMENT 41: Commenters suggested DNRC and/or board should take a portion of the grazing rental and set it aside to be used for improved monitoring and/or management of the lease, or that a portion should be given back to the lessee as a reward for improving the production of the lease.

RESPONSE 41: All revenues generated from grazing lands are annually distributed to the trusts except those monies deposited into the trust land administration account established under 77-1-108, MCA. Monies in this account are appropriated by the Legislature for management of state lands, and increases for monitoring and management would require legislative approval. By law and the Montana Constitution, diversion of revenues to lessees would not be allowed.

COMMENT 42: Commenter said the state should sell all scattered, underdeveloped parcels and utilize the monies for schools existing within the county of the sold property.

RESPONSE 42: Under the DNRC Land Banking Program, low-producing isolated parcels of state land are being sold. However, 77-2-337, MCA, provides DNRC direction on the distribution of sale revenues for specified trust beneficiaries and would prohibit returning those revenues solely to the schools that exist within the county where the lands were sold.

COMMENT 43: Commenters suggested FWP should contribute approximately 5% of their license fees or a portion of the license fee to the school trust since their wildlife grazes state land.

RESPONSE 43: DNRC is unaware of FWP paying any landowner for wildlife grazing. Additionally, wildlife belong to all the residents of the state, so utilizing only sportsman's license monies to pay such a fee would be inappropriate and outside the scope of this rulemaking.

COMMENT 44: Commenter said the rate should be based on lease productivity.

RESPONSE 44: DNRC determines stocking rates based on the productivity, topography, soils, and other factors of the land and as set by law. The rental is based on the carrying capacity. The fee charged from 1961 through 1991 did have an additional adjustment factor based on productivity; however, at DNRC's request that adjustment was removed as it was a disincentive to improve range condition.

COMMENT 45: Commenter said if the AUM fee was set at \$12/AUM, then the total amount a lessee could charge through a pasturing agreement would be \$24/AUM. The rate of \$24/AUM is too high.

RESPONSE 45: ARM 36.25.120(2) allows under a pasturing agreement, a lessee to charge a third-party livestock owner a management fee up to the current year's minimum grazing rate. The appropriate management fee is established by the lessee and livestock owner.

COMMENT 46: Commenter stated that a reduction to the AUM rate should not be granted based on improvements costs when the rancher owns these improvements and sells them when the lease agreement is transferred.

RESPONSE 46: 77-1-106, MCA, requires the board to consider lessee expenses for management, water development, weed control, and other costs when establishing rental rates.

COMMENT 47: Commenters stated the Duffield study strengths are that the multiplier takes into account the adjustment to the cattle market and that it recognizes that the federal rate is a subsidy.

RESPONSE 47: DNRC concurs that the Duffield study does present relevant information that the board can consider in reviewing the grazing rental rate. As previously stated, comments in the report regarding the federal rate were made based on a 2005 GAO report.

COMMENT 48: Commenter supported the proposed rate of \$12.88/AUM because it is similar to the rate of \$15.62/AUM used by the Department of Revenue (DOR) to establish grazing land values for property taxation.

RESPONSE 48: The private lease rate used by DOR is a seven-year Olympic average of private lease rates reported by the Montana Agricultural Statistics Service for the years 2001 through 2007. DNRC believes using the current Montana Agricultural Statistics Service private lease rate is appropriate with consideration given to costs as required under 77-1-106, MCA.

COMMENT 49: Commenter stated that ranchers who do not have a state lease would be happy to lease it for \$12/AUM and pay for improvements.

RESPONSE 49: DNRC appreciates the comment and agrees that there are ranchers in the state who are willing to pay a higher rate while paying the costs of improvements.

COMMENT 50: Commenter asked if the state was going to reduce mills charged for education if DNRC raises the AUM rate.

RESPONSE 50: The funding levels for public schools are established by the Legislature and by local governments, which is beyond the scope of this rulemaking.

COMMENT 51: Commenter stated DNRC should consider the leasehold value or cost to acquire the state lease in determining the fair market value of the AUM.

RESPONSE 51: Under ARM 36.25.118, assignments which result in a profit to the assignor over and above the value of improvements may result in cancellation of the lease. As such, DNRC does not consider use of leasehold interest appropriate in determining an appropriate multiplier. Additionally, leasehold value may be an indicator that the current rate is below market value.

COMMENT 52: Commenter suggested that DNRC should be comparing state lease AUM rates to federal lease AUM rates in order to remove the variables that are present in private leases.

RESPONSE 52: The board is required by law to ensure fair market value. The rental rate is to be set by taking the previous year's beef cattle price times a multiplier they establish in rule. The rate established by the federal Public Rangelands Improvement Act (PRIA) formula uses forage value index, beef cattle price index, and prices paid index, and does not have the requirement to achieve full market value that is required under Article X, Section 11 of the Montana Constitution. Due to these differences, DNRC does not believe it is appropriate to consider the PRIA rate.

COMMENT 53: Commenter stated that the Montana University System would directly increase their revenues by the increase in grazing rates.

RESPONSE 53: DNRC concurs. Grazing rentals are distributable revenues for the university system. Any rental increase would result in an increase in university revenues.

COMMENT 54: Commenters suggested that not all grazing revenues will be directly given to the school system.

RESPONSE 54: All grazing revenues generated on trust lands are distributed to the beneficiaries, except for that portion used to fund trust land management activities, and 5% of annual grazing revenues placed into the permanent fund as directed by Article X, Section 5 of the Montana Constitution. The funding level for the costs of trust administration is set by the Legislature through the biennial appropriation process.

COMMENT 55: Commenter said the original work of the 1991 Duffield and subsequent advisory board resulted in an approximate 45% reduction from the private lease rate. Since this figure was appropriate then, DNRC should continue to use the reduction figure and apply it to the new rate. If DNRC does not use the former reduction figure, then it should update the appropriate costs and expenses that are different in comparison of the private versus state.

RESPONSE 55: The 45% reduction resulted from the work of the advisory council using the private lease rate with deductions and additions to reflect the difference between state and private leases. DNRC initially recommended that the board use

the 2011 Duffield study as a basis to review the current multiplier. The 2011 Duffield Study recommended a 30% reduction. In setting the multiplier, the board has directed that additional reductions in the multiplier be made for weed control, to encourage rest-rotation grazing, to recognize that forage may be reduced by drought, and to allow for lower rental rates where the forage cannot be economically utilized.

COMMENT 56: Commenter stated concern with state lands intermingled within BLM lands. A fee increase would make it difficult to implement or maintain rest/rotation grazing systems; encourage lessees to graze each year regardless of resource conditions; encourage lessees to fence state lands from BLM lands and that those fences can impact wildlife movement; and that in pastures with steep topography and riparian areas, the riparian will be overgrazed because it may not be possible to utilize the forage in the steeper areas.

RESPONSE 56: As stated previously, DNRC feels the carrying capacity established on state lands is at a sustainable level that can be used every year. If lessees request to fence state lands separate from federal lands, DNRC will encourage use of wildlife-friendly fencing designs. For lands where topography may cause uneven utilization levels, DNRC will work with lessees to address any management issues that may develop.

COMMENT 57: Commenter suggested that instead of increasing the multiplier to raise revenue, DNRC should work with lessees on range renovations to increase the productivity and carrying capacity of grazing lands, which in turn will increase revenues.

RESPONSE 57: Although there may be opportunities for renovation projects, the basis for the proposed increase is to ensure that the rental being charged is full market value as required under the Montana Constitution.

COMMENT 58: Commenter suggested that Duffield's assertion that state lease rates are falling behind the increasing private rates is flawed because the increase in private rates is due to the increased costs to produce an AUM.

RESPONSE 58: While rising costs may be one reason for increasing private lease rates, others likely include weather conditions, availability, as well as increasing cattle prices.

COMMENT 59: Commenter stated that the decision to adjust the multiplier should not be based solely on the Duffield work.

RESPONSE 59: DNRC and the board considered information from the Duffield study as well as the public comments and data submitted, to make the adjustment to the proposed multiplier.

DEPARTMENT OF NATURAL RESOURCES AND CONSERVATION

/s/ Mary Sexton
MARY SEXTON
Director

/s/ Tommy Butler
Tommy Butler
Rule Reviewer

Certified to the Secretary of State November 28, 2011.